DEPARTMENT OF STATE REVENUE

SUPPLEMENTAL LETTER OF FINDINGS NUMBER: 06-0127
Sales and Use Tax
For Tax Years 2003-04

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ISSUE

I. Sales Tax—Imposition

Authority: IC § 6-2.5-2-1; IC § 6-3-2-1; IC § 6-8.1-5-1; 45 IAC 2.2-4-1

Taxpayer protests the assessment of sales tax.

II. Tax Administration—Negligence Penalty

Authority: IC § 6-8.1-10-2.1; 45 IAC 15-11-2

Taxpayer protests the imposition of a ten percent negligence penalty.

STATEMENT OF FACTS

Taxpayer operates a winter sports facility in Indiana. As the result of an audit, the Indiana Department of Revenue ("Department") determined that taxpayer owed additional sales tax for the tax years 2003 and 2004. Taxpayer filed a written protest and an administrative hearing was scheduled for August 1, 2006. Taxpayer did not attend the hearing, and the Department wrote and issued a Letter of Findings based on the materials in the file. Taxpayer requested a rehearing, stating that it did not receive notice of the hearing. The request for rehearing was granted and the rehearing was held on January 9, 2007. Additional supporting documentation was received on January 23, 2007. Further facts will be supplied as required.

I. Sales Tax—Imposition

DISCUSSION

Taxpayer protests some of the items upon which the Department issued proposed assessments. First, Taxpayer states that sales tax was paid on some of the items which the Department

determined were subject to sales tax. Second, Taxpayer states that some of the items listed as taxable were for services only, with no transfer of tangible personal property. Third, Taxpayer states that some of the purchases listed as subject to sales tax were not used by Taxpayer, but by related businesses. The Department notes that the burden of proving a proposed assessment wrong rests with the person against whom the proposed assessment is made, as provided by IC § 6-8.1-5-1(b).

Taxpayer's first point of protest is that sales tax was paid on some of the items which the Department included in the proposed assessments. As a part of this protest, Taxpayer has provided copies of receipts from some purchases. Some of those receipts show that sales tax was charged on those purchases. A supplemental audit of the file will be required to remove those purchases where sales tax has been collected from the amounts upon which sales tax should be collected. If the invoice or receipt does not show that sales tax was charged, that receipt or invoice does not meet the burden of proving the proposed assessment wrong, as required by IC § 6-8.1-5-1(b), and it will remain on the list of items which are subject to sales tax.

Taxpayer's second point of protest is that sales tax has been assessed on payments for services only. The relevant regulation is 45 IAC 2.2-4-1, which states:

> (a) Professional services, personal services, and services in respect to property not owned by the person rendering such services are not "transactions of a retail merchant constituting selling at retail", and are not subject to gross retail tax. Where, in conjunction with rendering professional services, personal services, or other services, the serviceman also transfers tangible personal property for a consideration, this will constitute a transaction of a retail merchant constituting selling at retail unless:
> (1) The serviceman is in an occupation which primarily furnishes and sells services, as distinguished from tangible personal property;
> (2) The tangible personal property purchased is used or consumed as a necessary incident to the service;
> (3) The price charged for tangible personal property is inconsequential (not to exceed 10[percent]) compared with the service charge; and
> (4) The serviceman pays gross retail tax or use tax upon the tangible personal property at the time of acquisition.
> (b) Services performed or work done in respect to property and performed prior to delivery to be sold by a retail merchant must however, be included in taxable gross receipts of the retail merchant.
> (c) Persons engaging in repair services are servicemen with respect to the services which they render and retail merchants at retail with respect to repair or replacement parts sold.
> (d) A serviceman occupationally engaged in rendering professional, personal or other services will be presumed to be a retail merchant selling at retail with respect to any tangible personal property sold by him, whether or not the tangible personal property is sold in the course of rendering such services. If, however, the transaction satisfies the four (4) requirements set forth in 6-2.5-4-1(c)(010),

> paragraph (1) *[subsection (a) of this section]*, the gross retail tax shall not apply to such transaction.

Taxpayer has provided sufficient documentation to establish that some of its payments were to an individual who edited video tape for a promotional video, and some payments were to an individual who created designs for various promotional items. In both cases, the payments were not for tangible personal property, but for services. The editor edited taxpayer's videotape. The designer provided a design, but no finished products which used those designs. Other businesses provided tangible personal property with the designs on them, and those purchases were subject to sales tax. As provided in 45 IAC 2.2-4-1(a), professional services, personal services, and services in respect to property not owned by the person rendering such services are not "transactions of a retail merchant constituting selling at retail," and are not subject to gross retail tax. Therefore, the payments made to the individuals who edited Taxpayer's videotape and who provided designs with no transfer of tangible personal property were not subject to sales tax.

Taxpayer's third point of protest is that some purchases listed as subject to sales tax on the audit report were purchased through Taxpayer, but that related businesses were the ultimate consumers. There is insufficient documentation to establish this position. Taxpayer has not met the burden of proving the proposed assessment wrong, as required by IC § 6-8.1-5-1(b).

Taxpayer also states that during the audit, it was informed that it had been collecting sales tax in error on locker rentals. As part of this protest, Taxpayer requested that the extra sales tax be credited towards its liabilities for this period. The Department cannot do this, since the sales tax which Taxpayer collected in error is not Taxpayer's to claim. IC § 6-2.5-2-1 explains:

> (a) An excise tax, known as the state gross retail tax, is imposed on retail transactions made in Indiana.
> (b) The person who acquires property in a retail transaction is liable for the tax on the transaction and, except as otherwise provided in this chapter, shall pay the tax to the retail merchant as a separate added amount to the consideration in the transaction. *The retail merchant shall collect the tax as agent for the state.* (Emphasis added.)

The sales tax was collected in error from Taxpayer's customers, and those customers are the ones who would need to file claims for refund. In other words, Taxpayer did not pay any sales tax, it collected and remitted sales tax, therefore the Department cannot refund sales tax to Taxpayer.

In conclusion, Taxpayer has provided documentation to show that some of the items which were purchased already had sales tax collected, and so should not be subject to sales tax again. Second, the videotape editing and designs did not result in the transfer of tangible personal property and is not subject to sales tax, as provided by 45 IAC 2.2-4-1(a). The sales tax collected in error was not paid by Taxpayer, and cannot be credited to Taxpayer. There is insufficient documentation to establish that taxpayer was not the ultimate consumer of the purchases listed in the audit report.

FINDING

Taxpayer's protest is sustained in part and denied in part.

II. Tax Administration—Negligence Penalty

DISCUSSION

The Department issued proposed assessments and the ten percent negligence penalty for the tax year in question. Taxpayer protests the imposition of penalty. The Department refers to IC 6-8.1-10-2.1(a), which states in relevant part:

> If a person:
> …
> (3) incurs, upon examination by the department, a deficiency that is due to negligence;
> …
> the person is subject to a penalty.

The Department refers to 45 IAC 15-11-2(b), which states:

> Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

45 IAC 15-11-2(c) provides in pertinent part:

> The department shall waive the negligence penalty imposed under IC 6-8.1-10-1 if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. In order to establish reasonable cause, the taxpayer must demonstrate that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed under this section.

In this case, taxpayer incurred a deficiency which the Department determined was due to negligence under 45 IAC 15-11-2(b), and so was subject to a penalty under IC 6-8.1-10-2.1(a). While Taxpayer has established that it does not owe some of the proposed assessments discussed in Issue I, Taxpayer has not affirmatively established that its failure to pay the remaining

deficiencies was due to reasonable cause and not due to negligence, as required by 45 IAC 15-11-2(c).

FINDING

Taxpayer's protest is denied.

WL/BK/DK March 5, 2007